



PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO
607 North 8th Street
BOISE, IDAHO 83702

MINUTES
OF
MEETING OF RETIREMENT BOARD

The Board of the Public Employee Retirement System of Idaho met at the PERSI Administration Building, 607 North Eighth Street in Boise, Idaho at 8:38 a.m., August 26, 2003. The following members were present:

Jody B. Olson
Susan K. Simmons
Dennis L. Johnson
J. Kirk Sullivan
Pamela I. Ahrens

The electronic projection of materials and documents discussed in the meeting was handled by Betsy Griffith. Executive Director Alan H. Winkle, Deputy Attorney General Brad Goodsell, Financial Officer James Monroe, Chief Investment Officer Robert Maynard, and Management Assistant Joanne C. Ax were also in attendance. Other persons attending portions of the meeting were:

Rod MacKinnon
Bill Palumbo
Drew Black
Dennis Fitzpatrick
Casey Maslonka
Charlie Brown
Doug Bates
Mike Boren
Chris Growney
Sue Curran
Mac MacBride
Matt Freeman

Mountain Pacific Investment Advisors
Mountain Pacific Investment Advisors
DB Fitzpatrick & Co.
DB Fitzpatrick & Co.
DB Fitzpatrick & Co.
REAI
Clearwater Advisors
Clearwater Advisors
Clearwater Advisors
Fidelity Investments
Fidelity Investments
LBO

Lucinda Smith
Susy Dees
Robert Schmidt
Ray Smith
Doug Dorn
Cecile McMonigle
Richelle Sugiyama
John R. Doner
Judy Aitken

Mellon
Mellon Russell
Milliman USA
Maximus
R.V. Kuhns
PERSI
PERSI
PERSI
PERSI

OLD BUSINESS

Approval of the Minutes: By motion duly made by Trustee Johnson and seconded by Trustee Simmons, the Board unanimously approved the minutes of the July 22, 2003, regular meeting of the Retirement Board as submitted. The minutes of the July 30, 2003 Investment Sub-Committee were then unanimously approved after a motion duly made by Trustee Simmons and seconded by Trustee Ahrens.

Mellon Trust Quarterly Update Mr. Maynard introduced visitors from Fidelity Investments, Sue Curran and Mac MacBride. Chairman Olson noted several changes in the order of agenda items and the presentations began with the Mellon Trust information. Noting that Wendy McCall has been promoted to another position in the firm, Lucinda Smith introduced Susy Dees as our Russell/Mellon Analytics representative going forward. The Board had previously received detailed copies of the second quarter 2003 performance report. Ms. Dees reviewed the total fund performance and that of domestic equity, global equity, real estate, international equity and fixed income. She said all asset classes have outperformed their benchmarks over the three- and five-year time periods. Still, compared to peers, PERSI ranked 65th and 42nd for those same periods within the TUCS Public Fund Master Trust Universe. Trustee Sullivan asked why trustees should feel good about rankings that are under the 50th percentile. Ms. Dees explained that our fund is underweight in Fixed Income and overweight in Equities relative to our peers; she further noted that PERSI managers are beating their benchmarks and are following the investment policy and allocation. Mr. Maynard further explained relative performance and peer rankings noting that PERSI managers were staying true to their agreed investment styles. Given our asset mix, the Total Fund performed better than expected.

Mercer Choice Plan Report: Mr. Maynard reviewed the detailed report which had previously been provided to the Board. 70% of investors remain in the Total Return Fund. Some who invest in the international equity fund appear to be timing the markets and moving in and out of the fund several times during the quarter. Generally, everything is performing as expected.

Since ING has been replaced, Mercer had not recommended any more changes. Following a difficult period, Brandes had a tremendous quarter which is typical of their style.

Monthly Portfolio Update: Mr. Maynard discussed his investment report dated August 24, 2003 which was an update from an August 18 version previously provided to the Board. In the report and in his discussion, Mr. Maynard noted the following:

The new fiscal year has started out on a positive note, bolstered by generally positive economic and corporate earnings news, but offset by a major increase in longer term interest rates and a sharp decline in fixed income returns.

All managers are either within their expected characteristics or have reasonable explanations for slight deviations. All managers are also performing within expectations given the markets.

The emerging markets and international portfolios have the best absolute performance, while TIPS have the worst. Zesiger, Schrodgers and TCW have the best relative performance for the fiscal year-to-date, while private equity, Genesis, MFS and Mountain Pacific have the worst.

The portfolio as a whole has, contrary to expectations, generally kept pace with the recent market turnaround helped in large part by the strong absolute and relative outperformance of the international, global, and emerging markets sectors. It remains to be seen if this good relative and absolute performance will continue.

Month-to-date returns were reported as 1.4% with a total fund value of \$6,712,490,322. This is an increase in market value for the fiscal year of \$165,320,267. Fiscal year-to-date returns are 2.3%.

Mr. Maynard recommended the immediate termination of Deutsche Asset Management and MFS. Mr. Maynard advised the Board that key personnel have left Deutsche Asset Management and consequently, immediate termination is recommended. In regard to MFS, revision in the investment process, coupled with their history of poor performance, warrant immediate termination. The manager termination process is to advise the Board and to then proceed unless the trustees have objections. Our custodian, Mellon, will be instructed to cut off access to account funds at the close of business today for those two managers. The MFS portfolio will be transitioned into The Russell 3000 index funds managed by Mellon Capital Management, which should keep costs low. The Deutsche portfolio has always been a low

turnover portfolio, and as such, it will be kept intact and monitored by Mellon Transition Management Services for the time being. There was further discussion as to how terminations are handled and how the investments are transferred. There was no objection from the Board to terminating these managers.

Mr. Maynard noted that when the markets were going down and we were outperforming, he was concerned that when they rebounded we would not be positioned to keep pace with the indices. So far, because of international exposure, since May 1 the markets have gone up 6.8% and our managers have made 8.8%. Outperformance of our global managers and international equities has kept us ahead of the rebound, which is encouraging.

Manager Comments: The Chairman invited managers who were present to comment on the markets and the economy. Clearwater Advisors believe interest rates will remain relatively flat – with perhaps a slight decrease in the short-term and an increase in rates further out. They believe the economy is trading on supply/demand, not fundamentals. Representatives from D.B. Fitzpatrick & Co. argue that the increase in rates last month was the sharpest in the decade and this was not due to technical factors, but rather, to economic fundamentals. They further noted that they were wrong in their pessimistic forecast of the Boise economy which has low vacancy rates in real estate and a stronger than anticipated economy. Mr. McGrath believes the last rate cut may have gone too far and Mr. Fitzpatrick expects the re-emergence of inflation in the next couple of years due to the effects of recent moves by Federal Reserve Chairman Greenspan. Bill Palumbo from Mountain Pacific Investment Advisors is concerned about the disparity between the perception of investors compared to that of business decision makers. Investors seem willing to take on a lot of risk, purchasing stock in companies that are not making any money; business decision makers seem unwilling to take on risk and they are hiring and spending very conservatively. Mr. MacKinnon added that this is the main reason why PERSI's domestic equity investments are underperforming. Consultant Doug Dorn said going forward we may want to change our international mandate to a global mandate.

Choice Plan Investment Policy: To allow more time for trustees to review the policy, Chairman Olson held the decision on the Choice Plan Investment Policy until the September Board meeting.

DC Plan Quarterly Statistic Report: Mr. Winkle reviewed the report previously provided to the Board by DC Plan Specialist Gay Lynn Bath. Answering a question from the Chair, Mr. Winkle said the average age of our participant is 48; those participating in private plans are about 8-10 years

younger. All age groups of PERSI members appear to be participating. In July, T.Rowe Price Small Cap Stock Fund replaced the ING Fund. At the same time, Admiral Shares replaced Investor Shares in the Vanguard Growth and Income fund resulting in lower investment fees for members. The transition went smoothly. The report showed a net increase of 474 contributors in the last seven months. About 8% of PERSI members are participating, contribution over \$1.35 million in July 2003.

FISCAL:

Update and Expense Reports: Financial Officer James Monroe had previously provided a memorandum dated August 18, 2003 to the Trustees which summarized current fiscal items of interest. Auditors from Deloitte and Touche are currently conducting the annual audit. Mr. Monroe reviewed the Administrative Budget report and the Portfolio Budget report in detail, explaining that most Portfolio fees are paid quarterly.

Unaudited Annual Financial Statements: Accountant Rhonda Yadon reviewed the unaudited financial statements for the quarter and year ended June 30, 2003 & 2002. The report included the allocation of all the assets by manager, a report of the Choice plan funds, sick leave funds and the PERSI base plan. Financial Officer Jim Monroe commended Ms. Yadon saying she has done an excellent job reworking the reports and compiling all the data. The format is consistent with GFOA standards.

EXECUTIVE DIRECTOR

Business Process Review Overview: Mr. Winkle introduced Consultant Ray Smith from Maximus who has been at PERSI about a month interviewing staff and beginning the BPR process. Mr. Smith reviewed the background of his company and consultants working on this project. Trustee Ahrens asked about imaging technology. Mr. Smith explained that the microfilm process currently used is a very old manual process and difficult to maintain. By using imaging, documents are digitized and can be linked so the user can access them instantly on the computer screen for reference. They can be sent electronically over the Internet or downloaded to a disk or CD for storage. Trustee Johnson said imaging is used in his company and understands that quality hardware is required to do imaging well. Mr. Smith said the assessment report will include any hardware that would be necessary to support all recommendations. The report will not only address imaging needs, but also what is needed to bring PERSI up to current financial industry standards.

Final Decision and Order – Alvin Petty Disability: Deputy Attorney General Brad Goodsell had provided a memorandum dated August 15 outlining the appeal of a final decision denying Mr. Petty's application for

disability retirement benefits. A hearing was held before a hearing officer on April 30, 2003 and a recommended decision was issued July 11, 2003. The recommended order found that Mr. Petty's application for disability retirement benefits should be approved. Trustee Johnson had carefully reviewed all the documentation and said it appears the appeal process is working properly. After initial denial by our third party administrator, VPA, the hearing officer had reviewed the matter and issued this recommendation. No exceptions were filed to the recommended decision. By motion duly made by Trustee Johnson, seconded by Trustee Simmons and unanimously approved, the Board adopted the recommended decision of the hearing officer in the contested case of In the matter of the disability retirement application of Alvin W. Petty, Case No. CC-02-03. The Recommended Order stated that it is the finding, conclusion and recommended order that the Petitioner receive PERSI retirement disability benefits in accordance with applicable state law and the rules and regulations of PERSI.

Amortization Schedule Discussion: Mr. Winkle had provided a memorandum dated August 18, 2003 to the Board. He reviewed the memorandum and said four major parts of the funding policy are to maintain a well-funded system, to keep contribution rates stable and not raise them unless there is a major change in circumstances, to maintain purchasing power through COLA's and to reduce contribution rates if it does not jeopardize the fund. The Board balances these items in making their funding decisions. Because we reached fully funded status, the former amortization schedule no longer applies.

The Board emphasized it wanted to be able to consider all factors when setting the COLA.

Status Update: Mr. Winkle reviewed the summary of PERSI projects report that had previously been provided to the Board. Chairman Olson thanked Trustee Simmons and Trustee Sullivan for serving on the consultant search committee. The RFP was released on August 25.

Review of the way schools award sick leave continues as well as how police officers, jailers and dispatchers are classified. Mr. Winkle met with Shoshone County and Representative Mary Lou Shepherd recently to discuss the dispatcher issue. Staff is surveying other counties and will meet again in December on this issue.

A record 533 members retired effective September 1, 2003. Growth in numbers of school teachers and baby boomers reaching retirement age seems to be driving the numbers. Our actuarial report should provide

interesting data as to whether our members are delaying retirement as in other systems.

Many peer retirement systems have severe funding challenges. Trustee Sullivan asked for any research in the industry concerning the cause of these problems to determine if it is from the economy or allocation or other reasons that might help educate us. Mr. Maynard said compared to our peers, the PERSI fund is in tremendous shape. Some of the problems are due to investment markets, which we should expect every 12-15 years. However, systems that sharply increased benefits when the markets were booming need as much as a 16% contribution rate increase now. Because PERSI kept a large reserve and provided a moderate amount for Gain Sharing, we need only to restore contribution rates to their 1997 levels, and that over a three-year period. Mr. Winkle added that many of the peer systems use a three to five-year averaging mode in their actuarial assumptions, so two very good years are still in the average; when they drop off, the numbers will be worse than they are now.

Mr. Maynard said as we select a new consultant, we may want to ask if they have the capability to research and present an industry overview of this issue in an organized form to the Board. Trustee Ahrens wants to ensure that budget analysts and others understand that our contribution rate increase is spread over three budget years. She asked Mr. Winkle to update the chart showing the costs of the contribution rate increase by employer group.

Chairman Olson asked Trustee Ahrens to review the Legislative Ideas which were presented as supplemental reading material to the Board

Future Board Meetings

Tuesday, September 30, 2003, 8:30 a.m., Boise – PERSI
Tuesday, October 21, 2003, 8:30 a.m., Boise – PERSI
Tuesday, November 18, 2003, 8:30 a.m., Boise – PERSI
Tuesday, December 16 2003, 8:30 a.m., Boise – PERSI

Adjournment: Chairman Olson said Trustee Johnson would be absent and excused from the September meeting. There being no further business before the Board, by motion duly made by Trustee Sullivan, seconded by

Trustee Johnson and unanimously approved, the meeting was adjourned at 11:00 a.m.

Jody B. Olson
Chairman

Alan H. Winkle
Executive Director